

# Generating Local Revenue by Taxing Telephone Services

Oroshaza, Hungary

## Background

Hungarian cities during 1990–1995 faced annual inflation rates exceeding 25 percent. At the same time, the central government was reducing subsidies to municipalities. Additionally, the central government was delegating previously performed national government functions to local governments without providing the financial resources to cover those services. Oroshaza (population 34,600), like many Hungarian communities, sought ways to increase local revenue to finance the city's essential services. Consequently, in 1995 Oroshaza adopted a local 1 percent industrial tax on the gross receipts of all local businesses except utility companies (i.e., telephone, gas, electric, and water service). Under national legislation adopted prior to 1989, publicly owned utility companies were exempt from the tax.

## Innovation

During preparation of the 1997 fiscal budget, the Oroshaza municipal budget staff considered ways to broaden local taxes. Attention soon focused on whether the local industrial tax could be applied to utility companies. Since 1989, telephone, gas, electric, and water companies have been privatized. These private companies were earning profits and were no longer owned by either the state or the City of Oroshaza. With privatization of utilities, investors and shareholders were benefiting from a tax exemption that was no longer appropriate. Oroshaza obtained a legal opinion clearly stating that municipalities could impose the local industrial tax on privately owned utility companies because these companies were no longer protected by the national legislation exempting public utilities from the industrial tax. Oroshaza subsequently adopted legislation applying the local industrial tax to telephone service.

## Results

In October 1996, the city received its first payment of the tax from the local telephone company. The 1996 total annual payment will be over 1 million Hungarian forints (US\$10,000). Presently only 10 percent of the homes in Oroshaza have phone service. Telephone services are expected to increase over the next two years, which will significantly increase revenues to the city. Additionally, whenever the telephone company wishes to increase local rates, the city will benefit. In the coming year, the Mayor and finance staff of Oroshaza may consider applying the local industrial tax to cable television, gas, and electric service. Adoption of these taxes will also provide a measure of protection against high inflation rates and declining subsidies from the central government.

## Summary

To help finance local services, the City of Oroshaza imposed a local industry tax on the privatized telephone company. Previously, utility companies were publicly owned and therefore not subject to the tax. In 1996 the tax will generate more than US\$10,000 in additional revenue for the city.

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